

STATE OF IOWA
DEPARTMENT OF COMMERCE
UTILITIES BOARD

IN RE: IOWA-AMERICAN WATER COMPANY	DOCKET NOS. RPU-2013-0002, TF-2014-0030
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ORDER REJECTING COMPLIANCE TARIFFS AND REQUIRING FILINGS

(Issued April 7, 2014)

On February 28, 2014, the Utilities Board (Board) issued its final decision and order in Iowa-American Water Company's rate proceeding (Iowa-American), identified as RPU-2013-0002. In its final order, the Board ordered Iowa-American to file compliance tariffs which, among other things, would recover all public fire costs and 25 percent of private fire costs through general metered services rates; the Board directed that half of these costs be recovered through the fixed monthly charge and half through volumetric rates.

On March 6, 2014, Iowa-American filed its proposed compliance rates. On March 11 and 18, 2014, Iowa-American filed additional information supporting its compliance filing.

On March 18, 2014, the Consumer Advocate Division of the Department of Justice (Consumer Advocate) filed a conditional objection to Iowa-American's compliance filing to allow more time for review. On March 27, 2014, Consumer Advocate filed an objection to Iowa-American's compliance rates. On March 31, 2014, Iowa-American filed a response to Consumer Advocate's objection.

Iowa-American proposed to recover the applicable fire-related costs through its customer charges based on number of customers instead of meter equivalents; the meter equivalents approach allocates costs based on the relative size of the customer. Iowa-American acknowledged that the Board's decision requires that 50 percent of the public fire costs and 12.5 percent of private fire costs are to be recovered through the customer charges and the remaining 50 percent of public fire costs and 12.5 percent of private fire costs are to be recovered through the volumetric rates, but Iowa-American argued that by allocating half of the recoverable costs to the volumetric charge, larger customers would be charged more because larger customers will typically consume more water.

Iowa-American said the balance of the costs should be allocated based on the number of bills as more costs have already been allocated to the larger customers through the volumetric rates. Iowa-American maintained that recovering these costs based on meter equivalents would effectively charge the larger customers twice based on their size. For example, Iowa-American said that a Commercial Customer with a 2-inch meter will be paying 8 times the fire contribution to the customer charge due to customer charges being based on meter equivalents. Iowa-American provided a table that shows two sets of monthly customer charges (one set based on the number of customers, which is the approach Iowa-American supports in its compliance filing, and the other based on meter equivalents) along with the proposed volumetric rates.

Monthly Customer Charges

	Based On No. of Customers	Base On Meter Equivalents
5/8"	\$14.08	\$13.36
3/4"	\$21.11	\$20.03
1"	\$35.19	\$33.39
1 1/2"	\$70.39	\$66.77
2"	\$112.62	\$106.83
3"	\$211.14	\$200.29
4"	\$351.90	\$333.82
6"	\$703.83	\$667.66
8"	\$1,126.10	\$1,068.24
10"	\$1,618.85	\$1,535.67

In its objection, Consumer Advocate said that Iowa-American's proposed compliance tariffs disproportionately affect residential customers based on how fire-related costs are being recovered. Consumer Advocate asked that the Board direct Iowa-American to spread the rate increase (including fire protection costs allocated to volumetric rates) evenly across all usage, and to calculate the monthly customer charge based on meter equivalents which results in a rate of \$13.36 for a 5/8-inch meter, with rates for other sizes scaled based on the 5/8-inch meter charge.

In its reply to Consumer Advocate's objection, Iowa-American argued that its proposed volumetric and customer charges are consistent with Iowa-American's compliance cost-of-service study and that Consumer Advocate's proposal would result in the allocation of a disproportionate and unreasonable amount of costs to the large water customers. Iowa-American said that customers generally benefit from public fire service commensurate with the size of their property and that, prior to the

Board's final decision in this case, cost recovery of 100 percent of public fire costs was based on meter equivalents, meaning that costs were recovered based on the relative size of the customer's premises.

With respect to the customer charge, Iowa-American said that customer charges based on meter equivalents produce lower customer charges, which shifts more cost recovery to the volumetric rates. Iowa-American argued that it is more equitable (and consistent with the American Water Works Association rate manual) to calculate monthly customer charges based on the number of customers.

Iowa-American noted that once the appropriate customer charge is calculated, the remaining fire-related costs must be recovered from the volumetric rates. As Consumer Advocate noted in its objection, Iowa-American said that the proposed compliance tariffs place more cost recovery on the first block of volumetric rates than the second block. Iowa-American stated that the change in the relative percentage increases in the first and second blocks is due to the change in the compliance class cost-of-service study based on the Board's determination on various revenue requirement, rate design, and cost-of-service issues. Because 97 percent of the residential class consumption is in the first block, Iowa-American said the first block should receive a larger increase than the other blocks.

Pursuant to the Board's final order, 100 percent of the public fire costs and 25 percent of private fire costs are to be recovered from all customers, with 50 percent of those costs to be recovered through the fixed charged and 50 percent through the volumetric charge. The total of fire protection costs recovered from all customers is

\$5,947,954. In Iowa-American's rate case filing, customer charges were based on meter equivalents. Now, Iowa-American wants to use number of customers, at least for customer charges associated with the fire protection costs paid by all customers. Generally, a methodological change of this magnitude in cost recovery should be addressed during the rate proceeding or rehearing process, not in compliance filings. As outlined below, Iowa-American's proposed change is inconsistent with the Board's final order.

Iowa-American's proposed method of recovering customer charges, based on number of customers, would result in recovery of \$3,216,745 per year of fire costs through the customer charge. Recovery using meter equivalents would result in recovery of approximately \$2,535,889. The use of meter equivalents provides recovery via the customer charge of almost half the fire costs, \$2,532,722, which are to be recovered from all customers. Iowa-American's rate case filing was based on meter equivalents and it is clear that use of meter equivalents more closely achieves the Board's directive to recover half of the costs through the customer charges. Iowa-American's compliance filing will be rejected and Iowa-American will be directed to file compliance rates that recover the applicable fire-related costs through the monthly customer charge based on meter equivalents as shown in Iowa-American's Attachment 1 – Alternative filed on March 18, 2014.

Iowa-American's proposed method for recovering 50 percent of the costs through volumetric rates recovers all applicable fire-related costs from the first two of its four rate blocks. The Board's final order did not limit recovery to only certain rate

blocks and some portion of the applicable fire-related costs should be recovered from each unit of water sold. Limiting recovery to the first two rate blocks essentially converts a volumetric or variable rate to a rate more closely resembling a fixed rate.

In Docket No. RPU-90-10, Iowa-American proposed to recover all public fire costs through a uniform adjustment to all volumetric block rates. Iowa-American contended that the volumetric method best matched fire exposure risks to fire protection costs, since there is a general relationship between water use and the amount of property exposed to fire. The Board agreed and directed Iowa-American to allocate those costs based on the base cost allocation factor in its cost-of-service study because it was the factor that most consistently measured general usage.

While the goal at some point might be for equal recovery from each unit of water, here that would result in a significant reallocation of costs between classes, based on the class cost-of-service study. Costs would decrease for the residential class and increase for the remaining classes with the industrial class experiencing the largest increase, resulting in an overall increase for the industrial class that exceeds the increase Iowa-American initially requested for that class. Therefore, the Board will not address the issue of uniform, per-unit recovery of applicable fire-related costs here but will defer consideration to a future rate proceeding, where the issue can be thoroughly addressed by all parties.

Nevertheless, the Board finds that it is appropriate to recover some portion of the applicable fire-related costs from each of Iowa-American's four rate blocks. The usage for the industrial class comprises almost 80 percent of the usage in blocks 3

and 4. Therefore, the Board will increase rate blocks 3 and 4 by, at a minimum, \$.0314 over the rates approved in Iowa-American's last rate proceeding, Docket No. RPU-2011-0001. This is a per-unit rate based on the total applicable fire-related costs and billing units for the industrial class, calculated based on half of the fire-related costs assigned to the industrial class (\$36,471) divided by total billing units for the industrial class (1,161,550). This approach provides that each unit of water will recover a portion of the applicable fire-related costs and moves Iowa-American's rates in the direction of uniform per-unit recovery. Iowa-American will need to make changes to the volumetric rates to reflect the lower monthly customer charges, and the recovery of fire-related costs from all rate blocks.

Iowa-American's filing also included proposed private fire service rates. The Board finds these rates to be appropriate and in compliance with the Board's final order in Docket No. RPU-2013-0002.

IT IS THEREFORE ORDERED:

1. The compliance filing made by Iowa-American Water Company on March 6, 2014, and supplemented on March 11 and 18, 2014, is rejected.
2. Within 20 days from the date of this order, Iowa-American shall file a compliance tariff with monthly customer charges calculated with the applicable fire-related costs based on meter equivalents, as detailed in this order.
3. Within 20 days from the date of this order, Iowa-American shall file compliance tariffs with revised volumetric rates that, at a minimum, increase rate blocks 3 and 4 by \$0.0314 per CCF over the rates approved in Docket No. RPU-

2011-0001, and that maintain the rate differential between rate blocks 1 and 2 to the maximum extent possible, as detailed in this order.

4. Within 20 days from the date of this order, Iowa-American shall file revised proof-of-revenue calculations based on the new rates.

UTILITIES BOARD

/s/ Elizabeth S. Jacobs

/s/ Nick Wagner

ATTEST:

/s/ Joan Conrad
Executive Secretary

Dated at Des Moines, Iowa, this 7th day of April 2014.